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Why Is Inflation So Low? - Speech by Richard Lambert to The Institute of Chartered Accountants of Scotland

Inflation as measured by the Consumer Price Index ran at just 1.1 per cent in the year to September, close to the lower threshold which would demand an open letter to the Chancellor of the Exchequer. This is despite rapid increases in the price of oil and other commodities, and a period of above average growth in the UK economy.

Is inflation really as low and stable as the CPI suggests? And what might happen to the path of inflation over the next two years? These are the questions addressed by Richard Lambert, a member of the Bank of England's Monetary Policy Committee, in a speech given at The Institute of Chartered Accountants of Scotland, in Glasgow, today.

Lambert dismisses the suggestion that the change of the target measure from RPIX to the CPI has somehow disguised an underlying change in the overall pace of UK inflation. More broadly, the low level of price increases during recent months is not just a UK phenomenon. Globalisation, new technology, deregulation and changes in the labour market have all contributed to an era of low and stable inflation across the developed world. Much improved management of monetary policy has also played an important role. And although temporary factors, such as weakness in food prices, are also affecting overall UK inflation, the weakness may also reflect structural changes such as increased competition in food retailing.

Looking ahead, he thinks the pressure of demand in the coming months may well turn out to be less intense than had been expected, and price pressures still seem quite muted in the supply chain.

But the impact of slower economic growth on inflation could at least partly be offset by the recent weakness in sterling and a flattening in the market yield curve. One big question concerns the outlook for the labour market, where inflationary pressures appear to have eased a little over the summer. Lambert says it is hard to find convincing explanations for why this should have happened.

Lambert concludes that inflation is indeed low and stable, and is set to remain so despite some swings in the prices of individual goods and services. "The likely path of inflation over the coming year is, however, uncertain", he says.

Key Resources

Why Is Inflation So Low? - Full Speech

<http://www.bankofengland.co.uk/archive/Documents/historicpubs/speeches/2004/speech230.pdf>